Internal Revenue Service

Department of the Treasury

Washington, DC 20224

200204049

S.I.N. 414.09-00

Contact Person:

Telephone Number:

In Reference to:

Date: OCT 31 2001

T:EP:RA:T2

Legend:

State A	=
Employer M	=
Plan X	=
Plan Y	=
Statute Q	=
Board R	=
Resolution O	=
Statute P	=
Group N Employees	=

Dear :

This is in response to a request for a private letter ruling dated November 17, 2000, as supplemented by a letter dated September 18, 2001, concerning the federal tax treatment of certain contributions made to Plan X and Plan Y under section 414(h)(2) of the Internal Revenue Code.

The following facts and representations have been submitted:

State A established Plan X and Plan Y, both of which you represent are qualified under section 401(a) of the Code. Employer M, an agency of State A, is a public institution of higher education that was established pursuant to Statute Q. Employer M is a participating employer in Plan X and Plan Y. Group N Employees of College M eligible to participate in Plan X and Plan Y are required to contribute to Plan X and Plan Y.

On September 18, 2001, Board R adopted Resolution O. Resolution O authorizes the

participation of Employer M in a pickup program pursuant to Statute P. Resolution O provides that Employer M will pick up, i.e. assume and pay, the mandatory Group N Employee contributions of Employer M's Group N Employees who participate in Plan X and Plan Y in lieu of such employees paying such contributions to Plan X and Plan Y. Resolution O further provides that no Group N Employee of Employer M has the option of choosing to receive the contributed amounts directly instead of having them paid by Employer M to Plan X and Plan Y.

Based of the aforementioned facts, you request the following rulings:

1. Contributions made by the Group N Employees who participate in Plan X and Plan Y which are picked up by Employer M pursuant to Resolution O will not be included in the gross income of the Group N Employees who participate in Plan X and Plan Y for federal income tax purposes.

2. Mandatory contribution amounts picked up by Employer M on behalf of the Group N Employees who participate in Plan X and Plan Y shall be treated as employer contributions and will not be includible in gross income of the Group N Employees who participate in Plan X and Plan Y in the year in which such amounts are contributed for federal income tax treatment.

3. No part of the mandatory contribution amounts picked up by Employer M will constitute wages for federal income tax withholding purposes in the taxable year in which they are contributed to Plan X and Plan Y.

Section 414(h)(2) of the Code provides that contributions, otherwise designated as employee contributions, shall be treated as employer contributions if (1) such contributions are made to a plan determined to be qualified under section 401(a), (2) the plan is established by a state government or political subdivision thereof, and (3) the contributions are picked up by the governmental employer.

The federal income tax treatment to be accorded contributions which are picked up by the employer within the meaning of section 414(h)(2) of the Code is specified in Revenue Ruling 77-462, 1977-2 C.B. 358. In that revenue ruling, the employer school district agreed to assume and pay the amounts employees were required by state law to contribute to a state pension plan. Revenue Ruling 77-462 concluded that the school district's picked-up contributions to the plan are excluded from the employees' gross income until such time as they are distributed to the employees. The revenue ruling held further that under the provisions of section 3401(a)(12)(A), the school district's contributions to the plan are excluded from wages for purposes of the Collection of Income Tax at Source on Wages; therefore, no withholding is required from the employees' salaries with respect to such picked-up contributions.

The issue of whether contributions have been picked up by an employer within the meaning of section 414(h)(2) of the Code is addressed in Revenue Ruling 81-35, 1981-1 C.B. 255, and Revenue Ruling 81-36, 1981-1 C.B. 255. These revenue rulings established that the following two criteria must be met: (1) the employer must specify that the contributions, although designated as employee contributions, are being paid by the employer in lieu of contributions by the employee, and (2) the employee must not be given the option of choosing to receive the contributed amounts directly instead of having them paid by the employer to the pension plan.

Revenue Ruling 87-10, 1987-1 C.B. 136, provides that in order to satisfy Revenue Rulings 81-35 and 81-36, the required specification of designated employee contributions must be completed before the period to which such contributions relate. Thus, employees may not exclude from current gross income designated employee contributions to a qualified plan that relate to compensation earned for services prior to the date of the last governmental action necessary to effect the pick up.

In this request, Resolution O satisfies the criteria set forth in Rev. Rul. 81-35 and Rev. Rul. 81-36, by providing, in effect, that Employer M will assume and pay the mandatory employee contributions of the Group N Employees who participate in Plan X and Plan Y in lieu of such employees paying such contributions to those plans and that the Group N Employees participating in Plan X and Plan Y have no option of choosing to receive the contributed amounts directly instead of having them paid by Employer M to either Plan X or Plan Y.

Accordingly, we conclude, with respect to ruling request one, two and three, that contributions made by the Group N Employees of Employer M who participate in Plan X and Plan Y which are picked up by Employer M under the provisions of Resolution O will be treated as employer contributions and will not be included in the gross income of the Group N Employees who participate in Plan X and Plan Y in the year in which such amounts are contributed for federal income tax purposes. These amounts will be includable in the gross income of the Group N Employees or their beneficiaries only in the taxable year in which they are distributed, to the extent the amounts represent contributions made by Employer M. Because we have determined that the picked-up amounts are to be treated as employer contributions, they are excepted from wages as defined in section 3401(a)(12)(A) of the Code for federal income tax withholding purposes. In addition, no part of the amounts picked up by Employer M will constitute wages for federal income tax withholding purposes in the year in which they are contributed to either Plan X or Plan Y.

These rulings apply only if the effective date for the commencement of the pick-up is not earlier than the date Resolution O was signed or the date the pick-up is put into effect.

For purposes of the application of section 414(h)(2) of the Code, it is immaterial whether an employer picks up contributions through a reduction in salary, an offset against future salary increases, or a combination of both.

These rulings are base on the assumption that Plan X and Plan Y meet the requirements for qualification under section 401(a) of the Code at the time of the proposed contributions and distributions.

No opinion is expressed as to whether the amounts in question are subject to tax under the Federal Insurance Contributions Act. No opinion is expressed as to whether the contributions in question are paid pursuant to a "salary reduction agreement" within the meaning of section 3121(v)(1)(B) of the Code.

This letter ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

Sincerely yours,

(signed) JOYCE E. FLOYD

Joyce E. Floyd
Manager, Employee Plans
Technical Group 2
Tax Exempt and Government
Entities Division

Enclosures:
Notice 437
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